FINANCIAL REPORTING BULLETIN

December 1998

Financial Reporting Division
Office of Research and Analysis
Office of Thrift Supervision
1700 G Street,, N.W., Washington, DC 20552

TFR DEADLINE MONDAY, FEBRUARY 1, 1999
CMR DEADLINE TUESDAY, FEBRUARY 16, 1999
It is important that you refer to this bulletin and the attached materials before submitting your December TFR.

ELECTRONIC FILING SOFTWARE YEAR 2000 COMPLIANT

Pursuant to the Year 2000 Information and Readiness Disclosure Act (Public Law 105-271, October 19, 1998), this is a Year 2000 Readiness Disclosure

Based on our internal testing, the electronic filing software provided to you this year by OTS for the preparation and transmission of Thrift Financial Report (TFR), including Schedule CMR, Cost of Funds (COF), and the Branch Office Survey (BOS) appears to be Year 2000 compliant. Nevertheless, it would be prudent for all institutions to also test the electronic filing software against their internal systems. If during testing, problems/issues are identified concerning the software, please contact Patrick G. Berbakos at 202-906-6720 or via the internet at patrick.berbakos@ots.treas.gov.

OTS does not contract for the development of HMDA electronic filing software, and, therefore, institutions should contact their HMDA software vendor directly to address these issues. For any other reporting requirements which are not mentioned here, institutions should contact the primary agency or software vendor responsible.

UPDATED SOFTWARE FOR DECEMBER

By the end of December, all savings associations should have received the December 1998 electronic filing software from DPSC, Inc. The updated version corrects errors in the previous version, adds and updates edits, and includes the annual filing of Schedule CSS, Subordinate Organization Schedule.

It is important that you install the most current software before preparing and transmitting your December reports. If you have not received the software update by December 31, please contact DPSC Customer Support at 800-825-3772.

FOURTH QUARTER REGULATORY REPORTS

The December 1998 TFR should be completed and submitted as soon as possible after the close of the quarter. All schedules except CMR are due no later than Monday, February 1, 1999. Schedule CMR is due no later than Tuesday, February 16.

If you have any questions concerning the preparation of your report, please call your Financial Reporting Division contact in Dallas, TX, or Trudy Reeves in Washington, DC, at 202-906-7317. If you have a problem with the electronic filing software or transmission, call Cheyann White at 972-281-2412 or Doris Jackson at 972-281-2052. If you need additional copies of the TFR form or instruction manual, call 202-906-6078, or obtain them from the OTS website at www.ots.treas.gov/ tfrpage.html.

1999 THRIFT FINANCIAL REPORT

The OTS has decided that it will make **no changes to the TFR for 1999** in order to allow thrift institutions to concentrate on year 2000 compliance issues.

OTS had proposed on Sept. 1, 1998, to collect additional information on the TFR, such as high loan-to-value lending data and to reorganize the TFR's equity section to display accumulated other comprehensive income, beginning with the first quarter of 1999.

However, after considering comments on the proposal and other factors, OTS decided to postpone any changes.

The 1999 TFR will be the same as the 1998 version, except for minor caption changes primarily to accommodate SFAS 133, "Accounting for Derivative Instruments and Hedging Activities." No lines in the form will be added or deleted and no field numbers will be changed. The following line caption edits will be made:

Schedule CF

CF360: Refinancing Loans

Delete the phrase "Included on Lines 190 thru 270 Above" because effective with the June 1998 TFR all refinancings are reported on this line even if no new funds are disbursed.

Schedule CCR

CCR102: Accumulated Losses (Gains) on Certain Available-for-Sale Securities and Cash Flow Hedges, Net of Taxes

CCR137: Accumulated Losses (Gains) on Certain Available-for-Sale Securities and Cash Flow Hedges

Include in the adjustment to capital and assets accumulated gains and losses on cash flow hedges, pursuant to SFAS No. 133, to comply with the interim guidance on the regulatory reporting and capital treatment for derivatives, which is scheduled to be issued in December 1998.

Schedule CMR

CMR, Form page 34, Heading: Financial Derivatives and Off-Balance-Sheet Positions

CMR, Form page 37, Optional Supplemental Reporting for Financial Derivatives and Off-Balance-Sheet Positions

Include with the off-balance-sheet positions, derivatives that are on-balance-sheet pursuant to SFAS No. 133. (See revised instructions for December 1998.)

DECEMBER CHANGES TO THE TFR INSTRUCTION MANUAL

Attached are 18 pages of the TFR Instruction Manual updated for December 1998. The revisions are indicated by a bar in the right margin.

Schedule CF - Mortgage Loans Disbursed: Added a clarification that all originations made in the name of the reporting association are to be reported, even if the loans are funded by a third party and immediately transferred.

Schedule CCR - Unrealized Gains on Available-for-Sale Equity Securities: Revised the instructions to clarify that unrealized gains are reported net of unrealized losses.

Conversion of LIP to Risk Weighted Asset - Clarified that to be converted at a 0% conversion factor LIP must be fully disbursed or expire in one year or less under the original terms of the contract.

Schedule CMR - Revisions Incorporating SFAS No. 133 - Added that the component of assets relating to accumulated gains and losses on assets subject to a qualifying fair value hedge should be reported with unrealized gains and losses on CMR508, 517, and 538. Derivative instruments in a gain position should be included in CMR544 (Miscellaneous II). The component of the carrying value of deposit liabilities and borrowings that consists of accumulated gains and losses related to qualifying fair value hedges should be included in CMR782 and

CMR784, respectively. Derivative instruments in a loss position should be reported in CMR787 (Miscellaneous II).

Information about financial derivatives and off-balance sheet contracts should be reported with off-balance-sheet contracts even if an institution has adopted SFAS No. 133.

SOFTWARE CORNER

Each quarter, this column addresses questions, problems, helpful tips, etc., regarding the OTS electronic filing software.

If you have a filing software topic you would like to see discussed in this column, please send your comments and questions to Doris Jackson via fax at 972-281-2002, or via the Internet at doris.jackson@ots.treas.gov.

NEW SOFTWARE

You should receive the December 1998 version of DPSC filing software by the end of December. If you have not received your new software by January 1, 1999, please contact DPSC Customer Service at DPSC, 800-825-3772, ext. 210.

CONVERSION TO WINDOWS

You can upgrade from the DOS to the Windows version of the filing software by contacting DPSC Customer Service at 800-825-3772, ext. 210.

CSS BY THE NUMBERS

With the December TFR, institutions will be filing Schedule CSS for the first time using the DPSC software. Because the 1998 software cannot bring forward last year's CSS data, this initial submission will require that the report preparer input information for <u>all active subordinate organizations</u> (including both consolidated and unconsolidated subsidiaries). The CSS edit has been expanded to assist with the completion of the schedule. To assist preparers with the completion of CSS, here is a step-by-step guide for Windows and DOS:

WINDOWS

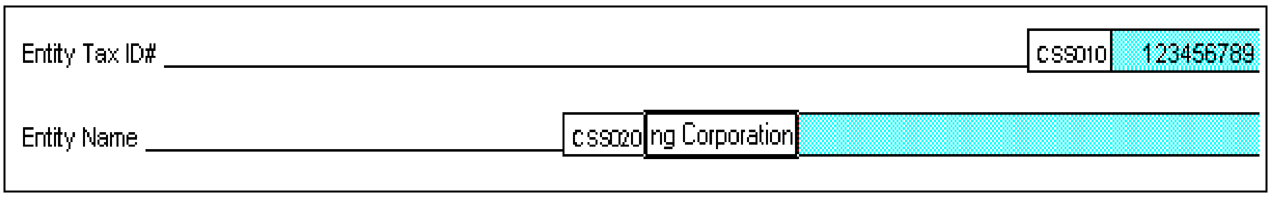
The following information can be found in Chapter 10 of the OTSReporter manual. Please refer to the manual if you have any questions.

1. If you are entering more than one subsidiary, check the box that says "Stay in CSS." This feature brings you back to the top of the schedule when you have completed data entry for an entity.

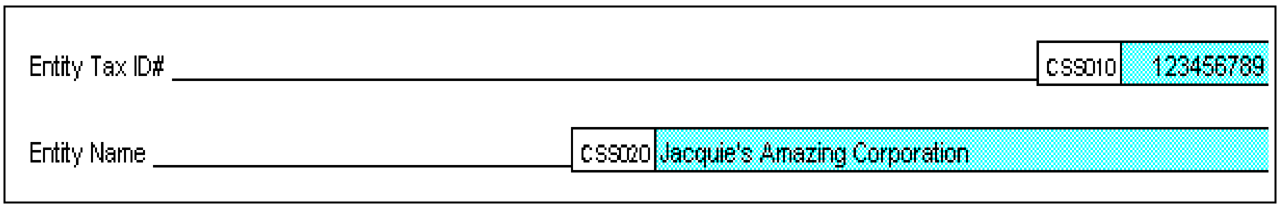
2. The drop-down box at the top of the schedule lists the information for each entity. All entries are prefaced by "(####)", which is a number sequentially assigned by the software. As you can see above, the software is ready to accept entry for the first subsidiary. DO NOT click the "Add New" button for the first entry! Just start with entering CSS010.

3. Some of the entry lines, such as entity name and address, have small cursor boxes in which the information scrolls as it is entered. Once you have advanced to the next line, the full entry appears correctly:

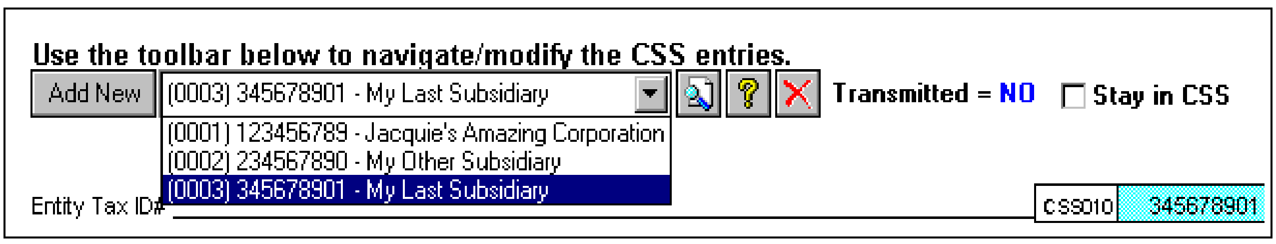
During entry:



After entry:



4. When you have completed an entry and the software has returned to the top of the schedule, click the "Add New" button. The subsidiary is assigned the next sequence number, and you may begin entry with CSS010.



5. Before entering the last subsidiary, click the "Stay in CSS" box to turn off the return feature. (See above.) When you have completed the last line of CSS, the software will continue with Schedule CCR.

In December 1999, the information entered in the December 1998 CSS should automatically roll forward. At that time you will only need to update the information that has changed and add or delete entities.

DOS

The following information can be found in Chapter 9 of the OTSReporter manual. Please refer to the manual if you have any questions.

1. CSS will be entered from the "Master Entry List" screen. This will automatically display after you choose to initialize Schedule CSS. The software will prompt you to do this.

2. You must press the F2 key to add an entity.

3. The cursor in the entry screen does not follow the CSS line numbers in order. For your reference, this is the sequence of entry"

   a. Entity Information (ID, name, address.)

   b. Financial Information (CSS120, CSS130, CSS140, CSS150, and CSS160.)

   c. Parent Information (ID and name only; the other information in this box refers to the entity.)

   d. Entity Information (business type and type of entity)

4. When you have completed entering a subsidiary, you must press the ESC key to return to the Master Entry List. You may then press F2 to enter a new subsidiary or ESC to return to the schedule selection screen.

QUESTIONS & ANSWERS

Q&A No. 45

SUBJECT: **Check Processing and Computer Center Co-ops**
LINE(S): Schedule CSS
DATE: December 10, 1998

Question: An institution owns small percentages (<5%) of both a check processing center and a computer center. Many other financial institutions are also stockholders. Should these two organizations be reported on Schedule CSS?

Answer: The answer to the question depends on what authority the thrift relies on to make the investment. If the thrift relies on its service corporation investment powers to make such investments, the entity must be included in Schedule CSS regardless of the ownership level. Alternatively, if a thrift relies on pass-through investment (§560.32) or its de minimis investment authority (§560.36) or some other thrift powers for such investments, then the entities are not considered subordinate organizations and, therefore, should not be listed on Schedule CSS.

Q&A No. 46

SUBJECT: **Definition of Real Estate Loans (TB72)**
LINE(S): SC250, SC253,SC316, SC340
DATE: December 10, 1998

Question: An institution is confused by the difference between the definition of real estate loans in OTS Thrift Bulletin No. 72 (TB-72) and the definition of mortgage loans in the TFR. The nonmortgage loan category in the TFR Instruction Manual includes loans based primarily on the credit worthiness of the borrower. However, the last paragraph on page 4 of TB-72, under the section titled "Abundance of Caution," states, a loan based on the creditworthiness of the borrower with an additional lien on the borrower's real estate (as an extra measure of protection), would be subject to real estate lending standards. This would seem to also require loans covered by TB-72 to be reported as mortgage loans. Are these loans to be reported as mortgage loans in Schedule SC?

Answer: The TFR classification of loans does not follow the real estate lending standards rule or TB-72. Therefore, a 1-4 family secured loan that does not fully qualify as a mortgage loan because the lender decided not to get an appraisal or because it is not fully secured by the real estate (i.e., has a loan-to-value ratio in excess of 100%) is classified on the TFR on SC310 through SC345. But this loan would still be subject to the real estate lending standards rule if it is secured by real estate as defined in 560.100-101.

All loans secured by, or financing the construction or improvement of, real estate are subject to the real estate lending standards rule (12 CFR 560.100-101). That means, the institution must establish prudent written lending standards that consider the interagency guidelines (attached to 560.101) and the supervisory loan-to-value (LTV) limits. If the institution makes loans with LTVs in excess of the supervisory limits, it should report them to their board of directors at least quarterly and limit such loans to 100% of capital for owner occupied 1-4 family mortgages and, within that limit, 30% of capital for all other high LTV loans.

Q&A No. 47

SUBJECT: **Trust Preferred Securities**
LINE(S): SC 185
DATE: December 10, 1998

Question: Where are Trust Preferred Securities reported on Schedule SC? OTS's TB-73 discusses these investment securities, and from reading it and the TFR instructions, I think they would be reported in SC185. The institution is currently reporting them on SC140. They have approximately $30 million of TPSs. The bulletin is clear that they are 100% risk weighted on CCR.

Answer: The following is quoted from TB 73:

> **Investment authority and limits for TPSs.** At this time, OTS believes that TPSs that otherwise meet the requirements of corporate debt securities set forth at 12 CFR 560.40 are permissible investments for federal savings associations.

Since the only TPSs that savings associations can invest in must meet the requirement of corporate debt securities, they should be reported on SC185, Other Investment Securities.

Q&A No. 48

SUBJECT: **Rabbi Trusts**
LINE(S): SO510
SO580
DATE: December 10, 1998

Question: An institution has accounts set up for a trust that its employees participate in. It is termed a "rabbi trust." Rabbi trusts are deferred compensation arrangements where amounts earned by employees are invested and placed in a trust. The institution is merely a conduit between the brokerage and the employee, with the employees solely responsible for contributions. The trust is reported by the institution in Other Assets. The directors and employees can buy or sell stock which the institution must mark-to-market, as a trading asset. The deferred compensation obligation is reported in Other Liabilities.

The question is: where would the income and expense related to the trust be classified in Schedule SO? SO510 refers to pensions "paid directly by the reporting association", and, therefore, the institution felt that SO510 is not appropriate.

Answer: Rabbi trusts are discussed in EITF Consensus No. 97-14. There are four scenarios for deferred compensation arrangements covered by this Consensus. This question relates to the type described in the Consensus as Plan D. In this scenario assets and liabilities of a rabbi trust are consolidated with the employer's financial statements because in the case of liquidation, the secured creditors would have rights to the trust assets. Assets held by the rabbi trust should be accounted for in accordance with GAAP for the particular asset (i.e., securities are accounted for under SFAS No. 115). The deferred compensation obligation should be classified as a liability and adjusted with corresponding charges (or credits) to expense (income) to reflect changes in the fair value of amounts owed to employees. The EITF consensus states that the income and expense as well as the asset and the liability should be reported separately. We would like to have all of these accounts reported in their appropriate "Other" categories on the TFR. Therefore, the expense should be reported on SO580 (Code 99).

Q&A No. 49

SUBJECT: **Conversion Factors For Lip**
LINE(S): CCR460
DATE: December 10, 1998

Question 1: Page 163 of the TFR Instruction Manual provides that LIP will be converted at the 0% conversion factor if - "(1.) LIP that contractually must be disbursed or expire in one year or less".

It appears that in the absence of a contractual obligation to disburse funds within a one-year period, the remaining term of a loan would generally determine whether it meets criteria #1, that the LIP contractually must be disbursed or expire in one year or less. For example, an 18-month construction loan which was originated 8 months ago, thus having a remaining term of 10 months, would satisfy this criteria because in less than 12 months it will be fully disbursed and if not, it would have to be repaid or renewed. In contrast, the same loan with a remaining term of 13 months would not meet the criteria, since the draws might not all be made until after one year had passed. Is this consistent with the intent of this provision?

Answer 1: According to the regulation, if the original maturity of a commitment is one year or less the conversion factor is zero. Generally, when the original maturity of the commitment exceeds one year, the conversion factor is zero only if (1) the institution has a contractual right to separately underwrite each disbursement and the institution does so, or (2) the institution has a contractual right to re-evaluate the lending relationship at least annually and the institution does so. Additional circumstances, but very limited circumstances in which a zero percent conversion credit factor apply are set out in 567.6(a)(2)(iv).

Question 2: If LIP will not be completely disbursed within one year, is the institution required to convert the entire balance at 50% or only that portion that is to be disbursed after one year? For example, assume a $10 million loan with an 18-month term. There are 14 months remaining and $2 million has been disbursed, leaving a $8 million LIP balance. According to the funding schedule, $7 million of the $8 million currently in LIP will be disbursed within 12 months. Would the institution have to convert the full $8 million LIP balance using the 50%

factor because the entire amount will not be disbursed within one year, or would it have to convert only $1 million, the amount which will remain undisbursed after one year?

Answer 2: The regulation does not contemplate splitting a single loan into a component which matures within one year and a component which matures later than one year. Instead, the maturity date of the loan is determinative.

Q&A No. 50

SUBJECT: **Liquidity Ratio for De Novo Institutions**
LINE(S): SI500
DATE: December 10, 1998

Question: Since there is no prior data to calculate the denominator, how does a De Novo institution report the liquidity ratio during their first reporting quarter?

Answer: A de novo that has no prior data with which to calculate the prior quarter's liquidity base may use current quarter information in both the numerator and the denominator of the liquidity ratio.

Q&A No. 51

SUBJECT: **Specific Reserves on Servicing Assets**
LINE(S): VA118
DATE: December 10, 1998

Question: An institution would like to know if it is appropriate to set up specific reserves on servicing assets at the time the asset is established.

On their books they debit "Gain or Loss on Sale" and directly credit the servicing asset. Conversely, on the TFR, Schedule SO, the Gain on Sale is grossed up, and SO570, Provision for Loss, is debited and a specific reserve on the servicing asset is credited. Hence, net Income is reported on the TFR in accordance with GAAP, but the provision for loss is not.

Is this correct?

Answer: No. Under GAAP it is not appropriate to set up a specific reserve at the time an asset is established; and, therefore, this would not be appropriate reporting on the TFR.

Q&A No. 52

SUBJECT: **Hypothecated Deposits - Downpayments on Construction Loans**
LINE(S): SC230
SC710
DATE: December 10, 1998

Question: Assume an institution closes a construction loan for $80,000. The borrower makes a $20,000 down payment to the institution, for which the institution credits LIP for $20,000. This transaction results in a negative $20,000 loan balance.

Is a down payment advanced by the borrower on a construction loan before any of the funds are disbursed, considered a "hypothecated deposit"? If so, should the hypothecated deposit be netted against the loan, or be classified on the other side of the balance sheet, as a deposit or escrow? If it is not a hypothecated deposit, where should the down payment be classified on the balance sheet?

Answer: Yes, this appears to be a hypothecated deposit. Since there is no loan balance to offset, it must be reported as a deposit.

Q&A No. 53

SUBJECT: **Brokered Deposits**
LINE(S): SI100
DATE: December 10, 1998

Question: An institution has unsolicited deposits from brokers, for which they do not pay a fee. Must these be reported as brokered deposits on SI100?

Answer: Yes. The deposits in question are brokered if the deposits meet the definitions of brokered deposit at 12 CFR 337.6(a)(2) (2) and the broker meets the definition of deposit broker at 12 CFR 337.6(a)(5). These cites are attached to this Q&A.

The fact that the deposits were not actually solicited by the institution has no bearing on whether the deposits should be classified as brokered deposits. It is a factual determination to classify brokered deposits, and it is the responsibility of each insured depository institution to accurately classify brokered deposits.

FDIC Interpretive Letter 92-73 specifically addresses this issue: "The key here is not whether the bank has solicited the funds, but whether the bank knows or has reason to know that the funds are being placed by a broker. If so, then the bank will be subject to any applicable restrictions on acceptance of brokered deposits based on its capital category. . . Mere knowledge on the part of your institution that it is accepting funds from a broker is sufficient to require that [Bank] be subject to the appropriate restrictions on brokered deposits for adequately capitalized banks.. . . In most instances, we would anticipate that banks, in the normal course of business, will be able to determine when funds are being placed by a broker."

SELECTED WEBSITE ADDRESSES

OTS Website Home Page: www.ots.treas.gov

FDIC Website Home Page: www.fdic.gov

TFR forms, the TFR Instruction Manual, and Financial Reporting Bulletins: www.ots.treas.gov/tfrpage.html

Quarterly aggregate thrift industry data: www.ots.treas.gov/quarter.html

Year 2000 Information: www.ots.treas.gov/y2k.html

FDIC-insured Institution and Industry Financial Information (Including Institution Directory and financial data for both savings associations and commercial banks, updated approx. 70 days after the reporting date): www.fdic.gov/databank/index. Html

The following can be accessed from: http://www.ots.treas.gov/ind-inst-data.html

- Cost of Funds
  - Current Report
  - Historical Data
- Thrift Industry National and Regional
  - Net Annual Chargeoffs by Asset Type
- OTS Fact Book (Historical Statistical Information of
  the Thrift Industry)

OTS Press Releases: www.ots.treas.gov/news.html

OTS New Directions Bulletins: www.ots.treas.gov/newdirections.html

OTS Regulatory Bulletins: www.ots.treas.gov/bltn_regulatory.html

OTS Thrift Bulletins: www.ots.treas.gov/bltn_thrift.html

OTS CEO Memos: www.ots.treas.gov/ceo-letters.html

OTS Legal Opinions: www.ots.treas.gov/opinions.html

OTS Final and Proposed Rules (past 12 months): www.ots.treas.gov/rules.html